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ABSTRACT

The fourth report in a series on school finance describes how state school finance formulas are differentiated and the calculations used to measure local need, wealth, and effort. The following topics are addressed: (1) criteria for evaluating state school finance programs; (2) origins of state school aid formulas; (3) operation of equalization formulas; (4) variables affecting state aid programs; and (5) impact of court-ordered reform on school finance. Charts explain how minimum foundation programs and the formulas for calculating percentage equalization aid work and how guaranteed tax bases and guaranteed tax yields affect formula outcomes. The conclusion of this report suggests that any proposal for changing funding formulas must consider the dynamics of the state-school district relationship that may enhance or limit the equalizing of fiscal opportunities and fiscal outcomes. (JAM)

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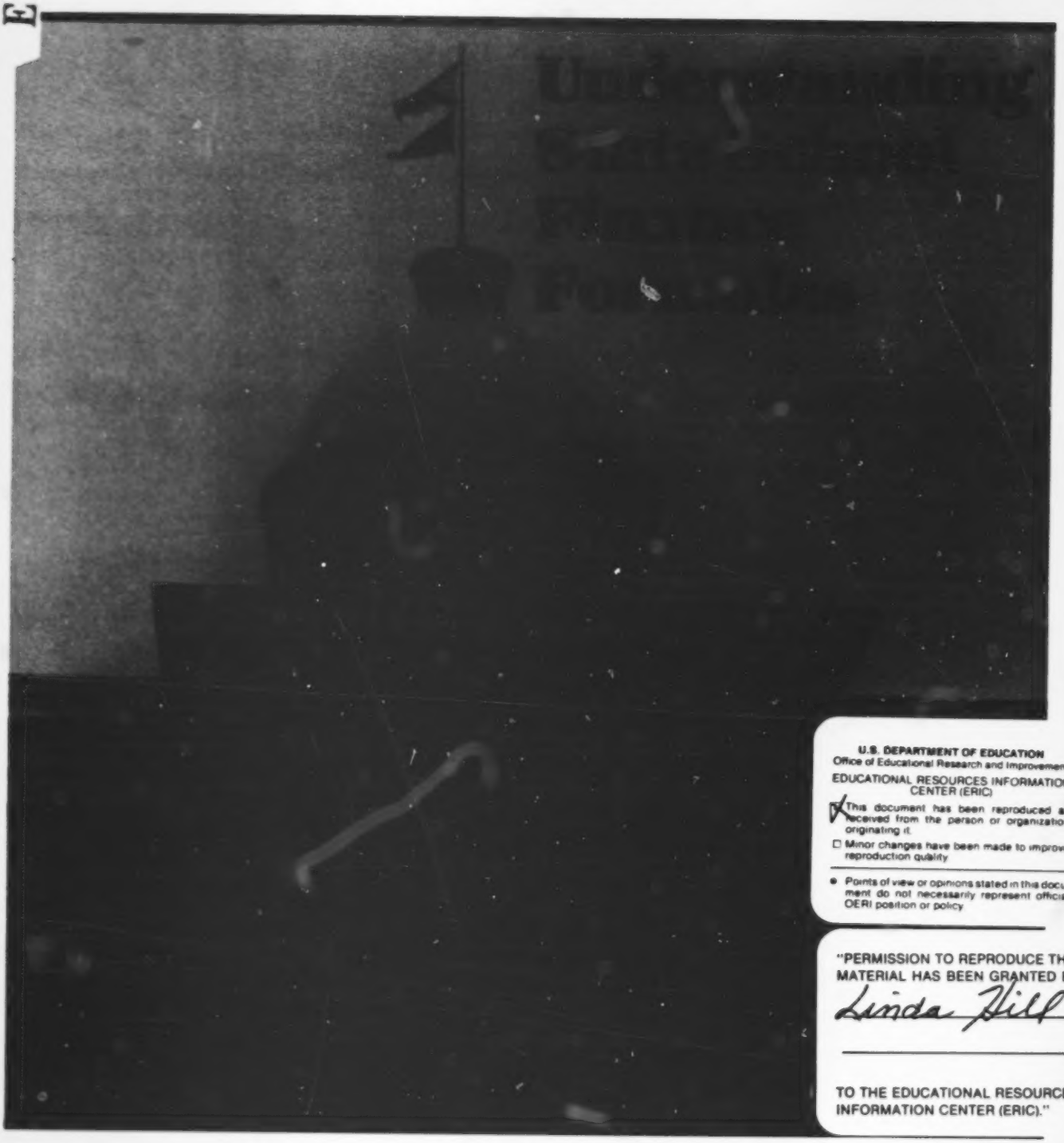

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Foreword

This publication continues NEA's series on school finance and the role of the local community. The issue of distribution of state funds becomes more important to NEA affiliates as the reform movement generates changes in school financing. It is therefore a necessity that affiliates become familiar with the workings of the various distribution systems available.

It will be shown that all present school aid formulas are mathematically equivalent. Differences among the states come about as a result of different methods for measuring local need, wealth, and effort. A knowledge of these differences will enable readers to assess, critique, and recommend changes in their state's formula.

Included in this report are sections on the following:

1. Criteria for evaluating state school finance programs.
2. Origins of state school aid formulas.
3. Workings of equalization formulas.
4. Variables affecting state aid programs.
5. Impact of court ordered reform on school finance.

Recommended guidelines and standards included in this report will help NEA affiliates with the difficult choices to be made concerning the method of distribution of state school funds. The report is a part of the action plan to implement recommendations contained in NEA's *Open Letter to America on Schools, Students, and Tomorrow*.

This manuscript was prepared by Peter Veillette of the Research staff. Inquiries concerning its contents may be directed to him.

Introduction

A Brief School Finance Primer

This "Search" publication is intended for use by all persons interested in school finance issues, not just those versed in its technicalities. With this idea in mind much of the specialized school finance jargon has been eliminated. Nevertheless certain terms and phrases remain either because they have precise meanings or because they lack an appropriate familiar synonym. Most such terms are defined when first used. The few that are basic to school finance and helpful to be known in advance are explained below.

On the revenue side, the local tax rate is called a *levy*. This levy is expressed in *mills*. The mill is a monetary unit equal to one-tenth of a cent. The tax levy expressed in mills is applied to each dollar of the *assessed value* of property. Assessed value represents the worth of the property as determined by the assessing authority. (Most jurisdictions routinely assess property at considerably less than its true market value.) The *tax yield* or liability is equal to the assessed valuation multiplied by the tax levy in mills. For example: property assessed at $100,000 and taxed at a 20 mill rate would be liable for $2,000 in taxes. ($100,000 x .02 = $2,000).

On the expenditure side, all state aid distribution formulas are based on concepts of *equalization*. In the lexicon of school finance, equalization comes in two varieties. First, there are state aid formulas that *equalize fiscal opportunities*. By this it is meant that the formula equalizes the ability of school districts to raise money. The second type of equalization formula will *equalize fiscal outcomes*. Those formulas equalize the number of dollars available to school districts on a per pupil basis. The mechanics of these school aid equalization formulas will be examined in the body of this text.

Counting of students can become confused in school finance formulas. States employ *average daily membership, weighted average daily attendance, October enrollment*, etc. as alternative counting methods. An understanding of the precise meaning of these terms is necessary to the study of a particular state's aid formula, but is not needed to understand the generic types discussed in this publication. Therefore the term *enrollment* is used here in place of any particular method of counting students for illustrative purposes in the formula examples.

Evaluating School Finance Programs

A question posed frequently in this time of education reform is: What is the best method for distribution of state education monies? The question is not new although the answer will vary depending upon one's perspective on the sometimes conflicting objectives of state aid programs. Notwithstanding these perceived differences, school finance writers have developed generally agreed upon principles for state school finance programs. One enumeration of these principles was published by the U.S. Commissioner of Education in conjunction with Public Law 93-380, Section 842 "Assistance to the States for State Equalization Plans." The law directed the Commissioner to develop a set of guidelines for states to use in evaluating the equity of their school finance plans. The guidelines were to be consistent with the Fourteenth Amendment which guarantees equal protection of the laws to all, and have equality of educational opportunity as their primary purpose. We can use these principles to assist in evaluation of state finance programs. The formulas employed by states as well as the overall state-local education finance scheme can also be tested against these standards. The principles are as follows.

School Finance Principles

Fiscal Neutrality

The principle of fiscal neutrality requires two conditions. First, tax burdens and tax efforts should be equalized among all school districts. Second, equal tax efforts should result in equal expenditures per pupil throughout the state, all other factors being equal. This principle has been accepted in courts as a legitimate test of school finance systems as far back as the 1971 California Supreme Court decision in *Serrano v. Priest*. In effect the court held that the quality of a child's education cannot be a function of wealth other than the wealth of the state as a whole.

Program Neutrality

The principle of program neutrality demands that the distribution of state funds should not result in an unintentional shift of financial support from one program to another. For example: a pupil weighting scheme understating the actual cost of special education programs could result in the district diverting funds from the regular instructional program to make up the difference.

Local Control

The principle of local control holds that decisions about educational fare and expenditures should be made at the school district level. It is as old as the public schools themselves, and rightly or wrongly, a major issue whenever school finance is discussed.

Equal Educational Opportunity

The principle of equal educational opportunity requires that every student have access to an instructional program appropriate to his or her potential. This dictum implies that the financing scheme not favor one student over another. The principle, however, does not require equal expenditures per pupil.

Financial Equity

The principle of financial equity requires that tax burdens not fall unequally upon classes of taxpayers.

Fiscal Variability

The principle of fiscal variability acknowledges that a state school finance system may have several dimensions; general and categorical aid, equalized and nonequalized aid. Nevertheless, while allowing for a variety of financial aid mechanisms, the system cannot completely ignore the other principles.

Political Feasibility

The principle of political feasibility means that a viable state aid program must balance the various elements in the foregoing principles. Political reality and necessity require that the state legislature construct an aid program which respects that balance.

Finance Formula Criteria

Besides these general principles for evaluating state school finance programs there are also very pragmatic criteria for evaluating school finance formulas. The list that follows was published in the Second Annual Yearbook of the American Education Finance Association. It appeared in an article by Orlando F. Furno and Dexter A. Magers, "An Analysis of State School Support Programs."

Objectivity

The data upon which the formula is calculated should be uniform and objective. There should be only one correct answer for each district's aid calculation.

Data Availability

The data for formula calculations should be easily obtained from local districts.

Practicality

The time and money required to compute aid and audit the data should be commensurate with the results. Districts should know what their aid will be at budget time.

Simplicity

The aid formula should be constructed in the simplest terms so that it might be easily understood.

Flexibility

The formula should make provision for accommodating cost variations due to changes in price and not changes in the quality and quantity of the program.

Economy and Efficiency

The distribution of funds should not require an excessive number of persons or expenditure of resources. Neither the state nor local districts should be overly burdened.

Fitting the Pieces Together

With such a fine list of principles and criteria it would seem that we could proceed to construct the "one best" state school finance program. Unfortunately this is not possible. Nevertheless the question as to why not a "one best" system deserves an explanation. The answer itself should help readers formulate their own ideas as to the best school finance system.

To construct the best school finance system one must first answer the philosophical question: Who has responsibility for financing the public schools? Is it a joint state-local venture? If so, who should be the senior partner? Perhaps you believe that the state should bear full responsibility for finance. Whatever particular financial mix you select will be reflected in the state aid distributions and formulas.

Having settled that fundamental issue it is now possible to establish a goal or goals for your school finance system. Do you want to equalize fiscal opportunities or equalize fiscal outcomes? In other words what should be the role of the state? If you choose to equalize fiscal outcomes you will design a system that treats all like students and taxpayers the same. Equal fiscal opportunity, in contrast, requires that equal tax efforts yield similar results in all districts. At this point it might be necessary to go back and check to be sure that the philosophy is consistent with the goal. For example, *a limited state financial role is inconsistent with equalization of resources.*

As a more practical matter it is necessary next to consider what is feasible given a state's particular fiscal sit-

uation and tradition. Has education been supported by the state at a high level? Does the state have a tax structure capable of supporting a high level of aid? Is local control of schools a dominant theme in discussions of change in the state aid program? What type of programs might be possible considering the makeup of the state legislature? What compromises can be anticipated?

A final stumbling block preventing the design of the "one best" state aid program is the variation in needs. Both the perception and definition of need will change reflecting the dynamics of demography and the desired educational fare. This is the point at which one must decide what shall be compensated for in the formula, how it shall be counted, and what value shall be assigned to it. As an example, you might decide to distribute state aid monies on the basis of classroom units, with a unit consisting of 20 students and one teacher, and the unit value being $25,000.

In summary, following the above steps (philosophy, goals, feasibility, and needs) we should be well on the way toward developing our own "best" state school finance system.

Origin of School Aid Formulas

The basics for all of today's state aid distribution formulas were developed between the years 1905 and 1930. In a sense it was an unlikely time for study of state aid to education since states contributed only about 15 percent of local school revenues. Yet that meager *state contribution lay at the heart of the problem: great disparities among the revenue generating abilities of local school districts.* To address that central problem, various aid plans were articulated by advocates whose names now are associated with them. A tour through those early years of school finance study will introduce the reader to four broad distribution plans available to states.

Flat Grants

The first stop on this tour is Teachers College at Columbia University. There, in 1905, Ellwood P. Cubberley completed his doctoral dissertation which many consider to be the first formal study of state school finance. Cubberley studied fiscal disparities that existed among school districts and ways the problem could be alleviated. He concluded that the state should distribute funds on a *flat grant* basis. Such a system would provide local districts with an equal number of dollars for each student in attendance plus an amount for each teacher employed. Cubberley also recognized that the poorest districts would need extra aid to help offset their weak tax-raising ability. He recommended a special fund be created for this purpose. *This flat grant system* of state aid proposed by Cubberley had two advantages. First, it *established a state-wide minimum program of financial support for all students.* Second, *it focused on educational needs by calculating aid on the basis of students and teachers. The main disadvantage of a flat grant aid program is that it does not equalize local ability to raise needed revenues.*

Foundation Programs

Before leaving Columbia University we encounter George D. Strayer, a professor and former classmate of Cubberley. In 1921 Strayer and a colleague named Robert M. Haig conducted a study of school finance for the State of New York. Their report, issued in 1923, found that the flat grants in use at the time were employed by school districts as a base upon which local funds were added. There was no mechanism in the program to equalize the resultant fiscal disparities. Therefore their recommended program emphasized fiscal equalization as opposed to the educational needs highlighted in flat grant programs. The *minimum foundation program* recommended by Messrs. Strayer and Haig would eventually become the most popular of all state aid distribution programs.

In theory a foundation program works like this: First, the state determines a minimum amount of money to be spent per pupil throughout the state. Next, the tax rate required to provide this minimum in the wealthiest school district is calculated. All districts are then required to tax at that rate. Finally, *the state commits itself to make up the difference between the dollars raised locally through the mandated tax and the dollars required by the state minimum*

foundation program. The principal advantage of a foundation program is that it provides a means of equalizing per pupil revenues independent of local property wealth. A potential disadvantage lies in the disequalizing effect of allowable local tax leeway above the mandated state requirement.

Not all would agree that local tax leeway constitutes a disadvantage to foundation programs. One such person, a student of Dr. Strayer, was Paul Mort. He believed that local leeway above the required levy was desirable to improve educational offerings. Mort argued that innovations financed by the leeway would eventually become incorporated into a state's foundation program thus allowing further innovation on the part of what he called "lighthouse" districts. In this manner continuous improvement of education would be encouraged. Mort eventually became the most effective spokesman for the minimum foundation program.

Percentage Equalizing

The next stop on the tour of early writers in school finance is the University of Pennsylvania. At the same time that Strayer and Haig were conducting their study at Columbia, Harlan P. Updegraff and Leroy A. King were studying similar problems in Pennsylvania. In their view foundation programs were flawed because the minimum level did not keep pace with rising costs of education, and local tax leeway only benefitted wealthy districts. They further believed the role of the state was to assist local districts in equalizing educational opportunities. This could be accomplished by equalizing local districts' fiscal capacity. In 1922 they proposed the state finance plan known as *percentage equalizing*, or state aid ratio. Under this system *the state reimburses a percent of local expenditures in inverse proportion to the district's property wealth*.

Here's how the system works. First the state determines what percent of total statewide expenditures it will finance. Next, local school districts decide what they will spend. At this point state aid ratios for each district are calculated using a formula combining wealth per pupil and the nominal state percent of expenditures. Finally, the aid ratio is applied to each school district budget to determine the amount of state aid. Two advantages are seen as accruing from a percentage equalizing state aid program. First, the formula is "fiscally neutral" in that the state payment will vary inversely to the amount of locally taxable wealth. Second, local control is promoted within a minimum to maximum range of expenditures allowed by the state. On the other hand, critics of this scheme argue that minimum expenditures mandated by the state are often less than a foundation program. Local districts don't always choose what the experts deem necessary. Another disadvantage occurs when a state must reduce its overall percentage contribution rate. Poorer districts, being more dependent on state aid, suffer a proportionately greater loss of dollars than do wealthy districts.

Percentage equalization is but one of several plans which have been developed to grant aid to school districts based upon a capacity equalization concept. Readers may be familiar with some of the others such as: guaranteed

tax base, guaranteed tax yield or district power equalizing. They are variations of the percentage equalizing formula based upon the work of Updegraff and King.

Full State Funding

The last stop on the tour of formative school finance writers is at the University of Chicago in 1930. Henry C. Morrison taught there and studied school finance programs, concluding that they all favored wealthy districts regardless of any equalization features. Morrison also believed it was the state that should control schools and design the curriculum. His solution therefore was to consolidate all local districts into one state-wide system. This single district would then be financed wholly by the state. A *full state funding* plan such as this would, of course, require a considerable increase in state revenues. Morrison proposed raising the necessary funds by means of a state income tax. Thus *a full state funding plan would have the advantage of achieving both taxpayer equity on the revenue side and student equity on the expenditure side.* A disadvantage to some, but certainly not to Morrison, was the loss of local control of schools. Although the plan has never been widely accepted, states continue to assume a greater responsibility for school financing.

The four systems of state aid listed below, flat grants, minimum foundation program, percentage equalizing, and full state funding form the basis of all fifty state finance programs. Differences among the states derive from variables which we shall examine. But first, it might be helpful to consider the mathematical formulas for the various types of equalizing grants.

SCHEMA OF STATE SCHOOL FINANCE PROGRAMS

Program Name	Equalization Effect
1. Flat Grants	Equal Dollars per Pupil
2. Minimum Foundation	Equal Dollars per (Pupil or Classroom) Unit
3. Full State Funding	Equal Call on State-Wide Resources
4. Capacity Equalization Programs	
A. Percentage Equalizing (State Aid Ratio)	Equalized Budget Portions
B. Guaranteed Tax Base	Equalized Tax Base per Pupil
C. Guaranteed Tax Yield (District Power Equalization)	Equalized Dollars per Mill Levied

How Do The Formulas Work?

Formulas for calculating equalization aid are often cluttered with add-ons, minimums, and other special provisions of state law which render them confusing. In their pure form, however, they are simple to calculate and easily understood. To illustrate this point we will look at the workings of four common equalization formulas: minimum foundation program, percentage equalizing, guaranteed tax base, and guaranteed tax yield.

The examples that follow show the application of these formulas to two school districts that we shall create; one with above average wealth, and the other with below average wealth. In all other aspects they are identical. Let us assume the following:

1. Both districts enroll 100 students.
2. The desired per pupil expenditure is $1,000.
3. The local tax levy is 10 mills, (expressed as .01).
4. Overall the state provides 50 percent of expenditures.
5. The poor district has $2,500,000 of taxable property.
6. The wealthy district has $7,500,000 of taxable property.

Minimum Foundation Program

Aid to school districts under a foundation program can be calculated using the following formula.

$$\text{Aid} = \left(\text{Enrollment} \times \begin{matrix}\text{Foundation}\\ \text{Expenditure}\\ \text{Per Pupil}\end{matrix}\right) - \left(\begin{matrix}\text{Local}\\ \text{Tax}\\ \text{Rate}\end{matrix} \times \begin{matrix}\text{Local}\\ \text{Assessed}\\ \text{Valuation}\end{matrix}\right)$$

Substituting appropriate values from our two districts, results in the following calculations for state aid:

Poor District	Wealthy District
Aid = (100 × 1000) − (.01 × 2,500,000)	Aid = (100 × 1000) − (.01 × 7,500,000)
Aid = 100,000 − 25,000	Aid = 100,000 − 75,000
Aid = 75,000	Aid = 25,000

The poor district with one-third the property wealth of the wealthy district receives three times as much state aid enabling it to spend the same amount per pupil with the same tax effort.

Percentage Equalizing

The formula for percentage equalizing distributions can be stated as follows:

$$\text{Aid} = \left(1 - \text{Local Percent of Expenditures} \times \frac{\text{Local Assessed Value Per Pupil}}{\text{State Average Assessed Value Per Pupil}}\right) \text{Total District Expenditures}$$

Our school district calculations follow in the table below. Thus our two districts would receive exactly the same amount of aid using this formula as using a foundation formula. Why? Because aid in both examples is being distributed in inverse proportion to property wealth.

Poor District	Wealthy District
$\text{Aid} = (1 - .5 \times \frac{25{,}000}{50{,}000})\ 100{,}000$	$\text{Aid} = (1 - .5 \times \frac{75{,}000}{50{,}000})\ 100{,}000$
Aid = (1 − .5 × .5) 100,000	Aid = (1 − .5 × 1.5) 100,000
Aid = (1 − .25) 100,000	Aid = (1 − .75) 100,000
Aid = (.75) 100,000	Aid = (.25) 100,000
Aid = 75,000	Aid = 25,000

Guaranteed Tax Base

Guaranteed tax base is a variation of percentage equalizing. The concept operates as follows. First the state establishes a guaranteed level of property valuation per pupil. Next, local districts subtract their tax base from the state guarantee level. The remaining amount is multiplied by the district's selected tax rate, and that product is multiplied by the number of pupils in the district.

The formula may be expressed as follows:

$$\text{Aid} = \left[\begin{matrix}\text{Local}\\ \text{Tax}\\ \text{Rate}\end{matrix} \times \left(\begin{matrix}\text{State Guaranteed}\\ \text{Assessed Value}\\ \text{Per Pupil}\end{matrix} - \begin{matrix}\text{Local}\\ \text{Assessed Value}\\ \text{Per Pupil}\end{matrix}\right)\right] \text{Enrollment}$$

For our two districts we may substitute as follows in the table below. Again our districts have fared the same as under the other equalization programs, demonstrating that the formulas are variants of a single distribution concept.

Poor District	Wealthy District
Aid = [.01 × (100,000 − 25,000)] 100	Aid = [.01 × (100,000 − 75,000)] 100
Aid = (.01 × 75,000) 100	Aid = (.01 × 25,000) 100
Aid = 750 × 100	Aid = 250 × 100
Aid = 75,000	Aid = 25,000

Guaranteed Tax Yield

This variation of the percentage equalizing formula is similar to the guaranteed tax base except that the state guarantees a tax yield per mill up to a maximum levy. It differs from a tax base guarantee in that the state may vary the tax yield depending on the selected tax rate, thus encouraging certain levels of expenditure. Local tax yield is subtracted from the state guarantee level.

The formula may be stated as:

$$\text{Aid} = \left(\begin{array}{l}\text{State Guaranteed}\\ \text{Expenditure at}\\ \text{Selected Tax Rate}\end{array} \times \text{Enrollment}\right) - \left(\begin{array}{l}\text{Local}\\ \text{Tax}\\ \text{Rate}\end{array} \times \begin{array}{l}\text{Local}\\ \text{Assessed}\\ \text{Valuation}\end{array}\right)$$

The formula is similar to a foundation program except that the local tax rate is selected by the district rather than being mandated by the state.

The table below shows how our districts fare under this plan. There are no surprises. All the equalization formulas can produce the same results. So long as our state chooses to distribute funds based upon an inverse relationship to local property wealth the outcome will be the same. Current distribution programs employed by states are shown in the checklist on page 16. Factors other than the mathematics of school finance formulas account for differences among states utilizing similar state aid systems. We will turn our attention to those differences next.

Poor District	Wealthy District
Aid = (1000 x 100) — (.01 x 2,500,000)	Aid = (1000 x 100) — (.01 x 7,500,000)
Aid = 100,000 — 25,000	Aid = 100,000 — 75,000
Aid = 75,000	Aid = 25,000

CHECKLIST OF PRINCIPAL STATE AID PROGRAMS

	Foundation Program	Guaranteed Tax Base	Guaranteed Tax Yield	Percentage Equalizing	Flat Grants	Full State Funding
Alabama	X					
Alaska	X					
Arizona	X					
Arkansas	X					
California	X					
Colorado			X			
Connecticut		X				
Delaware				X	X	
Florida	X					
Georgia	X					
Hawaii						X
Idaho	X					
Illinois	X	X			X	
Indiana	X					
Iowa	X					
Kansas			X			
Kentucky	X		X			
Louisiana	X					
Maine	X	X				
Maryland	X					
Massachusetts	X					
Michigan			X			
Minnesota	X					
Mississippi	X					
Missouri	X	X				
Montana	X		X			
Nebraska	X					
Nevada	X					
NewHampshire	X					
NewJersey		X				
NewMexico	X					
NewYork				X		
NorthCarolina	X					
NorthDakota	X					
Ohio	X					
Oklahoma	X		X			
Oregon	X					
Pennsylvania	X			X		
RhodeIsland				X		
SouthCarolina	X					
SouthDakota	X					
Tennessee	X					
Texas	X					
Utah	X		X			
Vermont				X		
Virginia	X					
Washington	X					
WestVirginia	X					
Wisconsin		X				
Wyoming	X					

Differences Among State Aid Programs

If there are only four basic equalization systems, then how do we account for differences beyond those basic classifications? Two types of variables are evident that will provide the answer. First, there are structural differences in the state-local fiscal relationship. Second, there are formula differences in the definition of local need, wealth, and effort.

Structural Differences

Among the first group, the most important is the percent of *school expenditures provided by the state.* No other factor *exerts so great an influence on the degree of equity in school finance programs.* Under any otherwise unencumbered distribution formula this is the key and represents the starting point for equalization. Presently the range among states is from a high of 90 percent in Hawaii to a low of 5 percent in New Hampshire. (See Table at end of this section.) The average for all states is 50 percent. Second only to the amount of aid provided by the state is the percent of state aid distributed through a general aid formula as opposed to distribution through categorical grants. A high level of state contribution distributed through a series of single purpose categorical grants serves the cause of equalization only secondarily. Under some conditions such grants can disequalize resources among districts. This would be the case if matching funds were required locally. In that situation the less wealthy districts would be less likely to participate. *Most states now tend to distribute between 70 to 80 percent of school funds as general aid, either equalized or as flat grants.*

Local leeway is a concept originally associated with foundation programs. What it means is that in addition to a required local tax levy, school districts are permitted to levy additional millage up to a specified maximum. This *local leeway tends to disequalize available resources among districts in direct proportion to locally taxable wealth.* The same tax rate will produce different revenues depending upon local property valuation. Notwithstanding this effect, it was local leeway that Paul Mort argued strenously for to provide the vehicle for educational improvement. Of course local add-ons can operate in the context of any state aid program, not just a foundation program.

Recapture is a concept usually associated with state guaranteed tax base/yield programs. Simply stated it *means that when a local tax levy yields funds in excess of the guarantee level, these funds are to be remitted to the state.* The state in turn uses these recaptured funds to help finance the program in districts below the guarantee level. In theory it has the same effect as would a state-wide property tax for school support. Theory or not, it has never been popular with taxpayers who view it as a confiscation of local monies to support other school districts. *To the extent that recapture is not incorporated into guarantee programs, disequalization is introduced to the detriment of less wealthy districts.*

State aid distribution schemes may contain save harmless provisions. These generally mean that no school district will receive less state aid than it received in the preceeding year regardless of formula calculations. The objective of such provisions is to smooth out

any sudden fluctuations in school support which would cause undue hardship for the district. Save harmless provisions also have a great deal of political appeal for obvious reasons. Nevertheless, the intent of equalization is corrupted by them. A variation of the save harmless provision is a state mandated minimum and in some instances maximum aid distribution. They owe their existence to the same political expedience reflected in save harmless clauses. In spite of their illogic, *minimum and maximum aid distributions give the impression that no district is being treated with excessive parsimony or generosity.*

Formula Differences

In addition to these structural differences affecting state aid systems, there is another group of differences; those pertaining to the formula. All equalization formulas contain three distinct factors: measures of local need, wealth, and effort. Previously, we looked at the formulas in their pure form. Now we will see the possibilities for variation brought about by differing determinations of need, wealth, and effort.

Measures of *local need* generally begin by counting something. It *may be pupils, teachers, classroom units, or a combination of those measures.* The choice of measure can have important equity implications. For example, choosing average daily attendance (ADA) over enrollment will work to the disadvantage of districts with high rates of absenteeism. In recent years it has become popular to assign weights to pupils in order to take into consideration the added costs associated with different grade levels, special education programs, vocational education, and the like. Whatever the unit counted, eventually this number is translated into a dollar amount representing the agreed upon state-local expenditure level. In our formula illustrations the local need was represented as $100,000.

The second aid formula variable is *local wealth.* This variable is arrived at by measuring something. The most common measure is the assessed value of local property, either the gross amount or the dollar value per pupil. Recently some states have modified this definition of wealth to include a measure of local income. Presumably this will yield a more accurate and valid measure of local wealth. Other possibilities include measuring sales tax collections, automobile registrations, and other nonproperty tax collections. However arrived at, the figure becomes an important part of the formula as it will be used to determine state and local shares of education expenditures. In the formula illustrations, wealth was either $2,500,000 and $7,500,000 for the two districts, or $25,000 and $75,000 per pupil in the districts.

The third variable included in state aid formulas is *local effort.* This is factored into calculations to determine the local contribution, or participation ratio in the case of a percentage equalizing distribution. Except for the percentage equalizing formula, the factor in our illustrations is .01 indicating a ten mill local tax rate. For the percentage equalizing illustration it is .5, indicating a total state-wide local participation rate of 50 percent. Perhaps more so than the other two factors, the local effort factor is crucial. Because it determines local contributions, it provides the key to all efforts toward equalization. As was stated previously: *the greater the state share the greater the equalization under the pure form of any state aid formula.*

In summary, we have two types of modifiers of state aid programs; structural differences in state-local fiscal relationships, and formula differences in need, wealth, and effort. These are the areas where legislatures enact adjustments which reflect each state's interpretation of equity in distributing education dollars.

PERCENT OF SCHOOL FUNDS FROM STATE SOURCES 1985-86

State	Percent	Rank	State	Percent	Rank
Hawaii	90.6	1	Tennessee	50.0	26
Washington	75.6	2	Ohio	46.3	27
New Mexico	75.4	3	Texas	46.0	28
Alaska	74.6	4	Pennsylvania	45.3	29
Alabama	73.4	5	New Jersey	44.7	30
California	68.7	6	Kansas	44.6	31
Delaware	68.7	6	Massachusetts	44.0	32
Kentucky	68.6	8	New York	43.9	33
Idaho	65.6	9	Rhode Island	41.9	34
North Carolina	64.2	10	Iowa	40.7	35
Oklahoma	64.1	11	Connecticut	40.5	36
West Virginia	63.8	12	Maryland	40.4	37
Arkansas	61.3	13	Wisconsin	39.8	38
South Carolina	58.9	14	Illinois	39.2	39
Indiana	58.2	15	Missouri	38.9	40
Mississippi	57.2	16	Wyoming	37.4	41
Georgia	55.8	17	Michigan	36.6	42
Utah	55.6	18	Virginia	36.1	43
Minnesota	54.4	19	Colorado	36.0	44
North Dakota	53.5	20	Vermont	35.6	45
Florida	53.4	21	Nevada	34.1	46
Arizona	53.3	22	Nebraska	28.1	47
Louisiana	53.2	23	Oregon	27.9	48
Montana	51.7	24	South Dakota	27.8	49
Maine	51.1	25	New Hampshire	5.0	50

Court Ordered Reform

For better than 15 years, legal challenges to state school finance systems have promised to cure the twin ills of inadequacy and inequity in funding public education. Scores of court cases have attacked state school aid programs on constitutional grounds. Through the years two points of attack have emerged.

The first of these is through the "equal protection" clause found in state constitutions. Plaintiffs argue that they constitute a class of persons being denied equal protection of the law because the financing scheme provides greater access to funds for those living in property wealthy school districts than those in property poor districts. The quality of one's education then becomes dependent on local wealth rather than wealth of the state as a whole. This violates the principle of fiscal neutrality.

A second point of attack is through state constitutional provisions requiring that states maintain a "thorough and efficient" system of education. Plaintiffs in poor districts argue that the results of the workings of the state aid system, plus local financial contributions, are great disparities in district resources and expenditures. This they claim to be a violation of the "thorough and efficient" mandate.

This two-pronged challenge to state school finance schemes attacks the structure of the system in the first instance and the outcome of the system in the second. Both approaches have been successful and both have failed in

court. The key to success seems to lie in a court's finding that education is a fundamental right under a state's constitution. When such a determination is made the court will apply the standard of "strict scrutiny" to the facts of the case. The less stringent "rational basis" test applies if such a determination has not been made. Under the strict scrutiny test the courts are much more likely to find that the financing system creates a "suspect class" and therefore unconstitutionally denies equal protection of the law to the plaintiffs. Similarly when the strict scrutiny test is applied to "thorough and efficient" provisions, the result is likely to be a mandate for a substantial equalization of financial resources.

To satisfy reform requirements states have responded with a variety of techniques. Some have increased the level of their foundation program while others have adjusted foundation formulas using pupil categories. Both solutions included a greater contribution on the part of the state. As was stated earlier, increased state funding using any distribution system tends to provide greater equalization. Two techniques involving the use of limits have also been employed in response to court ordered school finance reform. One type of limit acts upon growth rates of school district expenditures. By permitting higher rates of growth among the lower spending districts while holding down the growth rates of the highest spending districts, the overall system tends to come into balance. The other method involving state imposed limits sets a maximum on state payments under a guaranteed tax base formula, thereby eliminating the financial incentive for the local district to tax above a certain level.

Another method used to reform school finance has been to build a two tiered system. A state might start with a high level foundation program to assure a substantial degree of equalization. Added to this foundation is a state guaranteed tax base or yield program that allows districts the option to spend above foundation levels without sacrificing fiscal neutrality. This two tiered approach combines the two paths that have been taken to school finance reform; equal outcomes and equal opportunities. In the first instance a foundation program provides equal dollars for equal expenditure units with equal tax effort on the part of school districts. In the second instance state guarantee programs provide equal access to funds for equal district tax efforts.

The interesting thing about these responses to court ordered reform is that none of them represent new concepts or radical change from the old way of doing business. Because of widespread misinterpretation of early court decisions some had predicted the demise of ad valorem property taxes for school support. No such event occurred. The local contribution to school finance is still provided in the main by property taxes.

Perhaps we could say that what has been accomplished by the reformers is a speeding up of the rate of incremental change. States have increased their contribution to school financing. There exists less variation among districts in available revenues per pupil. There has been some fine tuning of the definitions of the "need," "wealth," and "effort" elements basic to all allocation formulas. However, as long as there is less than full state funding of education there will be disparities among school districts. Some perceive this as being a

good situation while others argue that it is wrong. These differences are fundamental, having their roots in the philosophies of the early advocates of various school finance systems. It is safe to assume that these differences will remain a part of the public dialogue about schools and their financing for the foreseeable future.

What Does It All Add Up To?

It was the purpose of this paper to eliminate some of the confusion and misunderstanding that surround school finance programs by demonstrating the underlying simplicity and similarity of the several formulas employed by states. In doing so, several tenets emerged that we can now summarize for use by NEA and its affiliates as points to consider in evaluating or formulating proposals for change. In addition to the principles enumerated at the outset, the following should be kept in mind:

- Different state finance systems exist because of different perceptions about the appropriate state-local relationship in financing schools.
- There are only four basic systems of general state school aid: flat grants, minimum foundation programs, capacity equalization formulas, and full state funding.
- As the state role becomes more dominant, fiscal disparities among school districts tend to decrease.
- All equalization formulas are based upon three factors: need, wealth, and effort.
- All equalization formulas can produce the same results assuming the three factors, need, wealth, and effort, are defined similarly in each formula.
- Formula variables, limits, and the state-local fiscal relationship account for differences that exist among states.
- School finance programs will change reflecting the realities of demography and the perception of educational need.
- Two approaches toward school finance reform are: equalizing fiscal opportunities, and equalizing fiscal outcomes.
- Reform efforts have tended to increase the amount of state aid and decrease the range of revenue disparities among school districts.
- Finally, in addressing the issues of school finance in its *Open Letter to America on Schools Students and Tomorrow*, NEA had this to say: "We believe state governments should institute reforms that would more equitably distribute the property tax burden among low-, middle-, and upper-income taxpayers." It stated further that "The NEA will support efforts by teachers and parents to convene forums and conferences that will plan and propose reforms in local taxation systems and state aid formulas." The principles enumerated in this report support those objectives.

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